



ARIZONA STATE SENATE
Fifty-Second Legislature, Second Regular Session

FINAL AMENDED
FACT SHEET FOR H.B. 2553

insurance; risk retention groups

Purpose

Establishes new rules and regulations for risk retention groups operating in the state.

Background

Current statute defines a risk retention group as a corporation or other limited liability association formed for the purpose of, and whose primary activity consists of, assuming and spreading all or any portion of the liability exposure of its group members (A.R.S. § 20-2401).

According to the National Association of Insurance Commissioners (NAIC), studies performed by the United States Government Accountability Office found that risk retention groups had a small but important impact in their niche markets, and were generally successful. However, the study also concluded there were some weaknesses, and risk retention groups would benefit from more consistent regulation by the states. This led to the formation of two NAIC working groups (the Risk Retention Working Group and the Risk Retention Group Task Force) to develop consistent guidelines for the states that eventually became accreditation standards.

The NAIC is an organization consisting of insurance regulators from the 50 states, the District of Columbia, and the five US territories. Though comprised of insurance regulators, the NAIC does not directly regulate insurance companies. Instead the NAIC establishes and reviews standards of best practices regarding insurance regulation at the state level. Model laws and regulations created by the NAIC are vetted and amended by member states before being adopted, but members are not required to adopt any model set forth by the NAIC.

There is no anticipated fiscal impact to the state General Fund associated with this legislation.

Provisions

1. Requires the board of directors of a risk retention group to consist of a majority of individuals independent of the group.
 - a) for reciprocal risk retention groups, the attorney-in-fact is required follow the same standards as the risk retention group; and
 - b) service providers of a reciprocal risk retention group must contract with a risk retention group and not the attorney-in-fact.

2. Specifies that an independent board director must have no material relationship with the risk retention group.
 - a) at least annually, a risk retention group must disclose to its regulator the criteria for determining independent board members; and
 - b) any person that is an owner of or a subscriber in the group, or is an officer, director or employee of an owner is considered independent unless some other position constitutes a material relationship.
3. States that the term of any material service provider contract with a risk retention group may not exceed five years.
 - a) a contract renewal must receive the approval of the majority of the board of directors.
4. Allows the board of directors to terminate any service provider, audit, or actuarial contract at any time provided adequate notice is given.
5. States that a service provider contract is deemed as material if the payable amount for the contract is greater than or equal to five percent of the risk retention group's annual gross written premium, or two percent of its surplus, whichever is greater.
 - a) a service provider contract that is deemed material may not be entered into unless the Director of the Department of Insurance (Director) is notified in writing of the intention within 30 days, and the Director has not disapproved the contract.
6. Requires the board of directors to adopt a written policy outlining a plan of operation that does the following:
 - a) ensures that all owners or insureds receive evidence of ownership interest;
 - b) develops a set of governance standards;
 - c) oversees the evaluation of the risk retention group's management;
 - d) reviews the amount to be paid for all material service providers; and
 - e) reviews all of the following at least annually:
 - i. the group's objectives relevant to compensation of officers and service providers.
 - ii. the performance of the officers and service providers.
 - iii. the continued engagement of the officers and material service providers.
7. Requires each risk retention group to maintain an audit committee composed of at least three independent board members.
8. Stipulates that a non-independent board member may participate in the audit committee, but cannot be a member of the committee, and must be invited.
9. Requires the audit committee to adhere to a written charter that does all of the following:
 - a) assists in overseeing the integrity of financial statements, legal and regulatory requirements;
 - b) discusses annual and quarterly audited financial statements with management, and its independent auditor;
 - c) discusses policies with respect to risk assessment and management;
 - d) meets separately and periodically, either directly or indirectly, with management and independent auditors;

- e) reviews any audit problems with the independent auditor;
 - f) sets clear hiring policies; and
 - g) requires the external auditor to rotate primary responsibilities and reviewing responsibilities, so that one individual does not perform audit services for more than five consecutive years.
10. Allows the board of directors of a risk retention group to fulfill the requirements of the audit committee with the discretion of the Director.
11. Requires a risk retention group to post the following information electronically:
- a) the process by which the board of directors are elected;
 - b) the board director qualification standards;
 - c) the board director responsibilities;
 - d) the board director's access to management, and independent advisors as necessary;
 - e) the board director's compensation;
 - f) the board director's orientation and continuing education;
 - g) the policies for management succession; and
 - h) the policies and procedures followed for annual performance evaluation.
12. Requires the board of directors to adopt and disclose a code of business conduct that covers all of the following:
- a) conflicts of interest;
 - b) matters covered under the Corporate Opportunity Doctrine under the state of domicile;
 - c) confidentiality;
 - d) fair dealing;
 - e) protection and proper use of a groups assets;
 - f) compliance with applicable laws, rules and regulations; and
 - g) reporting any illegal or unethical behavior that affects the risk retention group.
13. Requires the captive manager, President, or Chief Executive Officer of a risk retention group to notify the domestic regulator of any material noncompliance with any governance standards.
14. Requires the Director, beginning on or before December 31, 2017, to annually report the following to the President of the Senate and the Speaker of the House of Representatives:
- a) the number of risk retention groups licensed in this state;
 - b) any regulatory action taken against a risk retention group for noncompliance with statute;
 - c) the number of private passenger automobile insurance policies that were non-renewed during the previous calendar year;
 - d) the number of private passenger automobile insurance policies in force at the end of the previous calendar year; and
 - e) the number of private passenger automobile insurance policies in force within the state's assigned risk plan at the end of the previous calendar year.
15. Specifies that the Director may provide reports in electronic format.

16. Defines *board director* as a natural person designated in the articles in the risk retention group, or designated, elected or appointed by any other manner, name or title to act as a board director.
17. Defines *board of directors* or *board* as the governing body of the risk retention group elected by the shareholders or members to establish policy, elect or appoint officers and committees and make other governing decisions.
18. Defines *material relationship* as a person's relationship with the risk retention group, including:
 - a) the receipt of an amount greater than or equal to five percent of the risk retention group's annual written premium, or two percent of its surplus, in any 12-month period of compensation;
 - b) an affiliation or employment with a present or former, internal or external auditor; and
 - c) a relationship with a board director or immediate family member of a board director who is employed as an executive officer of another company where any of the risk retention group's present executives also serve on the board of directors.
19. Defines *service providers* as captive managers, auditors, accountants, actuaries, investment advisers, attorneys and managing general underwriters.
20. Makes technical changes.
21. Becomes effective on the general effective date.

Amendments Adopted by Committee of the Whole

- Adds an annual reporting requirement pertaining to the Director.

House Action

INS 2/17/16 DP 8-0-0
3rd Read 2/24/16 56-3-1

Senate Action

FI 3/16/16 DP 6-0-1
3rd Read 4/13/16 30-0-0

Signed by the Governor 5/11/16
Chapter 201

Prepared by Senate Research
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FB/ZD/rf